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June 15, 2007

VIA HAND DELIVERY

Mr. Charles L. A. Terreni
Chief Clerk and Administrator
Public Service Commission of South Carolina
Post Office Drawer 11649
Columbia, South Carolina 29211

RE: Application of Alltel Communications, Incorporated for
Designation as an Eligible Telecommunications Carrier
in the State of South Carolina
Docket No.: 2007-151-C

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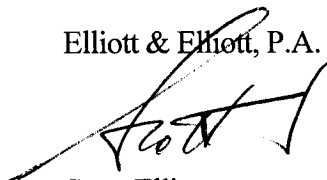
Dear Mr. Terreni:

Enclosed please find the original and twenty-five (25) copies of the Testimony of Dr. Brian K. Staihr filed on behalf of Embarq in the above referenced docket. By copy of this letter, I am serving all parties of record. I have enclosed an extra copy of this testimony which I would ask you to date stamp and return to me via my courier.

If you have questions, please do not hesitate to contact me.

Sincerely,

Elliott & Elliott, P.A.


Scott Elliott

SE/jcl

Enclosures

cc: All parties of record w/enc.
H. Edward Phillips, Esq.

RETURN DATE: OK D. Duke
SERVICE: OK D. Duke

**TESTIMONY OF
DR. BRIAN K. STAIHR
ON BEHALF OF
UNITED TELEPHONE COMPANY OF THE CAROLINAS
d/b/a/ EMBARQ**

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1 *Please state your name, title and business address.*

2

3 My name is Brian K. Staihr. I am employed by Embarq Corporation as Director-Policy /
4 Regulatory Economist in the Department of Law and External Affairs. My business
5 address is 5454 W. 100th Street, Overland Park, Kansas 66211.

6

7 *On whose behalf are you testifying in this proceeding?*

8

9 On behalf of United Telephone Company of the Carolinas d/b/a/ Embarq (hereafter
10 referred to as the "Company").

11

12 *Please briefly describe your educational background and work experience.*

13

14 I hold a B.A. in Economics from the University of Missouri-Kansas City, and an M.A.
15 and Ph.D. in Economics from Washington University in St. Louis. My field of
16 specialization is Industrial Organization, including Regulation.

17

18 Embarq is the company that was created when Sprint-Nextel "spun-off" its local
19 exchange operations in May of 2006. United Telephone Company of the Carolinas is
20 part of those operations. I began working with Sprint's Regulatory Policy Group in 1996.

1 In my current position I am responsible for the development of state and federal
2 regulatory and legislative policy for Embarq. I am also responsible for the coordination
3 of policy across business units. My particular responsibilities include 1) ensuring that
4 Embarq's policies are based on sound economic reasoning, 2) undertaking or directing
5 economic and quantitative analysis to provide support for Embarq's policies, 3)
6 advocating those policies in state and federal proceedings, and 4) conducting original
7 research. The specific policy issues that I address include universal service, pricing,
8 costing (including cost of capital), access reform, reciprocal compensation and
9 interconnection, local competition, marketplace issues, and more.

10
11 In the eleven years since the passage of the Telecommunications Act of 1996 I have
12 testified before Congress on telecommunications issues, and my research has also been
13 used in congressional oversight hearings. I have appeared before the Commissions or
14 Boards of the following states: South Carolina, Virginia, Florida, Kansas, New Jersey,
15 Pennsylvania, North Carolina, Nevada, Texas, Illinois, Missouri, Georgia, California,
16 New Mexico, Minnesota, and Nebraska. I have also worked extensively with the staff of
17 the Federal Communication Commission ("FCC") and have presented original research
18 to the FCC.

19
20 In January 2000 I left the telecommunications industry temporarily to serve as Senior
21 Economist for the Federal Reserve Bank of Kansas City. There I was an active
22 participant in the Federal Open Market Committee process, the process by which the
23 Federal Reserve sets interest rates. In addition, I conducted original research on

1 telecommunication issues and the effects of deregulation. I returned to the industry in
2 December 2000.

3
4 For the past twelve years I have also served as Adjunct Professor of Economics at Avila
5 University in Kansas City, Missouri. There I teach both graduate and undergraduate
6 level courses.

7
8 Prior to my work in regulation I served as Manager - Consumer Demand Forecasting in
9 the marketing department of Sprint's Local Telecom Division. There my responsibilities
10 included forecasting the demand for services in the local market, including basic local
11 service, and producing elasticity studies and economic and quantitative analysis for
12 business cases and opportunity analyses.

13
14 *What is the purpose of your testimony?*

15
16 The purpose of my testimony is to address the Application of Alltel Communications,
17 Inc. ("Alltel") for Designation as an Eligible Telecommunications Carrier ("ETC") filed
18 with the Public Service Commission of South Carolina ("the Commission" or
19 "Commission") on April 18, 2007. Specifically, my purpose is to offer suggestions and
20 recommendations as to the manner in which the Commission should approach and
21 evaluate not only Alltel's ETC application, but also all other pending and forthcoming
22 ETC (C-ETC) applications.

1 *Why is it appropriate for Embarq to offer suggestions and recommendations to the*
2 *Commission as to how ETC applications should be evaluated?*

3
4 The Commission recently issued a Commission Directive in which it was established that
5 the FCC's guidelines for ETC designation would serve as a guiding—but not
6 controlling—factor in its considerations of ETC applications. In that directive the
7 Commission also stated that “the public interest should be paramount in our
8 considerations.”¹ With regard to the public interest, in the FCC's ETC Designation Order
9 from 2005 the FCC was explicit that state commissions may wish to apply their own
10 criteria to public interest determinations beyond the criteria contained in the FCC's
11 guidelines.² In fact, the FCC indicated that state commissions were “...particularly well-
12 equipped to determine their own ETC eligibility requirements.” Therefore, as an
13 incumbent provider in South Carolina it is appropriate for Embarq to raise issues that we
14 believe are key to the public interest in South Carolina and suggest that the Commission
15 give particular weight to these issues as it uses the FCC's guidelines as a “guiding—but
16 not controlling” factor.

17
18 *Do you have specific recommendations about guidelines that the Commission should use*
19 *in evaluating the Alltel application and other ETC applications?*

¹ Commission Directive in Docket No. 2006-37-C, May 30, 2007.

² FCC Report and Order in CC Docket 96-45 released March 17, 2005 (“ETC Designation Order”), paragraphs 58-64. Throughout this testimony all references to legal documents including orders, decisions, rules, etc. are an economist's reading of the order, rules, etc. and are made specifically with respect to the economic implications of the reference. Any references to legal documents or references to sections of legal documents are not intended to be put forth as legal interpretations.

1 Yes. Embarrq, the Office of Regulatory Staff, and Alltel jointly filed comments regarding
2 proposed regulations for designating ETCs which the Commission filed with the
3 Legislative Council on March 26, 2007. Our comments, filed June 1, 2007, included
4 suggested revisions to the proposed regulations.

5
6 *Can you summarize the suggested revisions and the issues they address?*

7
8 The jointly filed revisions take steps toward requiring that any applicant commit to
9 fulfilling all service requests unless the Office of Regulatory Staff determines, after
10 investigation, that a specific request is unreasonable. This represents much-needed
11 movement toward achieving greater regulatory parity among ETCs in that it represents
12 movement toward carrier of last resort responsibilities that are currently fully-shouldered
13 by local exchange companies like Embarrq but not by C-ETCs. The jointly filed revisions
14 also would require that a public interest test include comparisons of customer density in
15 LEC wire centers and sub-wire center areas where an applicant intends and does not
16 intend to provide service using its own facilities. The customer density test would offer
17 some assurance that the applicant would not engage in blatant cream skimming.³ In
18 addition, the recommendations would require a newly designated ETC to report annually
19 on its continued reliance on resale and the feasibility of migrating customers served
20 through resale to the newly-designated ETC's own network. Embarrq has consistently
21 held that new ETCs should be required to use USF dollars to expand their networks in

³ Cream-skimming can exist both within a single wire center and across wire centers. When a C-ETC uses its own facilities to serve low-cost portions of a wire center and relies on resale to serve the higher-cost portions of the same wire center it is avoiding the costs of serving the high-cost areas just as certainly as if it had not offered service in the high-cost areas at all.

1 and into high cost areas of a state, which goes to the very purpose of universal service
2 fund support. While the joint revisions do not preclude reliance on resale, the
3 Commission could use the information from such reporting to determine whether a
4 provider's continued ETC designation remains in the public interest. Finally, the jointly
5 filed recommendations would require an ETC applicant to include in its service
6 improvement plan a detailed discussion of how it intends to expand its network to un-
7 served and under-served areas for which it seeks ETC status. Again, this addresses
8 Embark's position that universal service fund support should be used to provide facilities-
9 based choices in high cost areas of the state. While the jointly filed recommendations do
10 not explicitly require such build out, the Commission will at least have evidence of an
11 ETC applicant's intentions and give those intentions proper weight as it considers
12 whether initial and continued ETC status is in the public interest.

13
14 *Is Alltel's ETC application based on the jointly proposed revisions?*

15
16 Alltel's application is based on the FCC's existing ETC rules and was filed before the
17 jointly proposed revisions were developed. Because Alltel helped develop and agreed to
18 the jointly proposed revisions, I would expect Alltel to revise its application to conform
19 to them. I would also expect Alltel to file with the Commission and make available to all
20 parties in this proceeding its service improvement plan. I would encourage the
21 Commission to carefully review Alltel's service improvement plan to ensure that any
22 universal service fund support it might receive is used for intended purposes.

1 *Do you have reason to believe that Alltel would not use universal service fund support to*
2 *expand its network into un-served and under-served areas of the state?*

3
4 No. Embarq knows with certainty that Alltel—unlike many other wireless carriers—has
5 in fact used USF dollars to build out into un-served areas in other states. However, while
6 it is likely that Alltel would do the same in South Carolina, it is important that the
7 Commission assure itself of Alltel's intentions by carefully reviewing a service
8 improvement plan that includes its intentions to expand its network. And going forward,
9 it is even more important that the Commission assure itself in this manner for wireless C-
10 ETCs that do not have Alltel's history of using USF dollars to expand coverage.

11
12 *Is it Embarq's position that Alltel's application in this proceeding should be denied?*

13
14 No. It is Embarq's position that the Commission needs to take additional steps with
15 regard to all C-ETC applications that will help to ensure the public interest is served in
16 South Carolina.

17
18 *You have touched on the issues the jointly filed revisions would address. Can you*
19 *elaborate as to why these are important public policy considerations?*

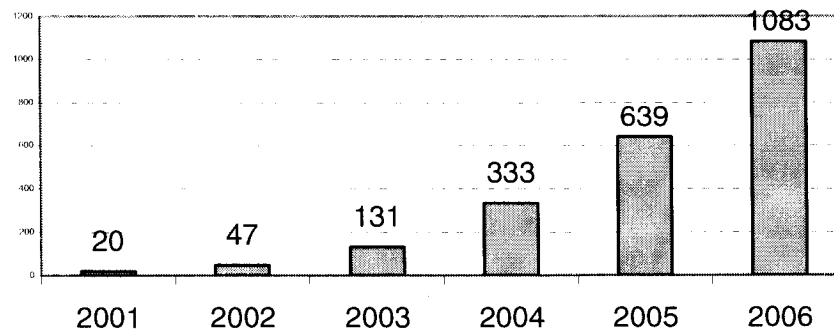
20
21 Let me begin by describing the current environment in which the Commission should
22 evaluate all applications for ETC designation. Simply put, with regard to universal
23 service the world is a very different place than it was only a few years ago. Currently the

1 FCC and the Federal-State Joint Board on Universal Service (“Joint Board”) are
2 immersed in the middle of an ongoing, complex proceeding to try and resolve significant
3 problems that exist within the federal universal service fund. These problems include—
4 but are not limited to—an alarming increase in the growth of the fund over the past four
5 years that has been caused by granting competitive ETC applications.

6
7 *Is there any question at all that this problem of excessive fund growth has been caused by*
8 *C-ETC applications?*

9
10 There is no question at all. The graph below depicts data taken from a graph that FCC
11 Chairman Kevin Martin presented at a recent Joint Board *en banc* proceeding.⁴

C-ETC Receipts - Millions Annually



12
13 As the table shows, C-ETC receipts from the Federal USF fund have grown from \$20M
14 annually in 2001 to over \$1B annually in 2006. At the same time, receipts going to
15 incumbent firms such as Embarq *have not grown at all* in the past four years. This
16 relationship is depicted the first graph of Attachment BKS-1. Attachment BKS-1

⁴ Presentation of FCC Chairman Kevin Martin before at the Federal-State Joint Board on Universal Service
En Banc Proceeding, February 20, 2007, Washington D.C.

1 contains copies of the actual graphs that Chairman Martin presented at the Joint Board *en*
2 *banc* proceeding.

3
4 *Why exactly is this growth a problem?*

5
6 There are two reasons. First, because ultimately all USF dollars come out of the pockets
7 of consumers. Companies collect the dollars they turn over to the Federal USF by
8 assessing end-users through a line item on the end-user's bills. That line item, based on a
9 contribution factor calculated by the Universal Service Administration Corporation
10 ("USAC"), increases as the need for fund dollars increases. In 2002 the contribution
11 factor was 6.8%. In 2004 it was 8.7%. In May of 2007, it was 11.7%.

12
13 The second reason is this: In many cases the dollars that have caused this excessive
14 growth are not being used, as one might imagine, to build out telecommunications plant
15 in underserved, high-cost areas. As I said earlier, experience has shown that Alltel is an
16 exception in this regard. But in many other instances the dollars are going to wireless
17 carriers for serving the exact same areas that four or five other wireless carriers are
18 already serving. For example, in the state of Mississippi there are currently over half a
19 dozen different wireless C-ETCs receiving dollars for providing service *in the exact same*
20 *study area*.

21
22 *But aren't these wireless C-ETCs required to take their USF dollars and expand their*
23 *coverage areas?*

1 No they are not, and that is an important point for the Commission to keep in mind as it
2 evaluates ETC applications and related service improvement plans. Under the current
3 rules no wireless C-ETC is required to use USF dollars to expand its coverage into un-
4 served or underserved high-cost areas. This is discussed in more detail below. As I have
5 explained, even the jointly filed revisions do not include such a requirement. However,
6 they do call for a detailed description in service improvement plans about how the
7 applicant intends to expand. They also call for annual reports about continued reliance
8 on resale, both of which are improvements over the status quo.

9
10 *Returning to the issue at hand, how should the Commission use this information as it*
11 *evaluates all ETC applications?*

12
13 The Commission has a public interest determination that it must make when evaluating
14 any ETC application. This is true whether the application is for an area served by a rural
15 incumbent or by a non-rural incumbent.⁵ The important point for the Commission to
16 keep in mind is that this public interest determination is a multi-faceted and complex
17 decision. Granting any ETC application goes well beyond a perfunctory “checking-of-
18 boxes” that the applicant has met a certain list of criteria. It also goes beyond a simple
19 desire for increased competition. On that point, the FCC has been very clear; in its
20 Virginia Cellular Order the FCC wrote: “We conclude that the value of increased

⁵ Over the years there has been a significant amount of debate as to whether state commissions were required to make explicit public interest determinations in all ETC applications, or just those applications for serving areas served by rural incumbents. The FCC clarified this with its 2005 ETC Order in which it stated, “Under Section 214 of the Act, the Commission and state commissions must determine that an ETC designation is consistent with the public interest, convenience and necessity.” (FCC Report and Order in CC Docket 96-45 released March 17, 2005.)

1 competition, by itself, is not sufficient to satisfy the public interest test in rural areas.”⁶

2 In fact, the entire nature of the decision that is currently before the Commission was
3 nicely summarized by (then) FCC Commissioner Kathleen Abernathy in the Virginia
4 Cellular Order released in 2004:

5 “While promoting competition is undoubtedly a core goal under the
6 Telecommunications Act of 1996, the use of universal service funding to
7 engender competition where market forces alone cannot support it presents a
8 more complex question. Particularly in rural study areas, where the cost of
9 providing service typically far exceeds retail rates, regulators must carefully
10 consider whether subsidizing the operations of an additional ETC promotes the
11 public interest... While at one point the cost of granting ETC status to new
12 entrants may have appeared trifling, the dramatic rate of growth in the flow of
13 funds to competitive ETCs compels us to consider the overall impact of new ETC
14 designations on the stability and sustainability of universal service.”⁷
15

16 *Is Alltel seeking ETC designation in rural study areas in South Carolina (as mentioned in*
17 *the above quote)?*

18
19 Yes it is. According to the application Alltel seeks to be designated an ETC in more than
20 twenty (20) rural telephone company service areas.

21
22 *Is there anything else about the current USF and C-ETC environment that the*
23 *Commission should consider?*

24
25 Yes, two things. First, under existing rules C-ETCs do not have to meet the same
26 requirements that incumbent firms such as Embarq must meet as carriers-of-last-resort.

⁶ Memorandum Opinion and Order in CC Docket 96-45 (“Virginia Cellular Order”), released January 22, 2004, paragraph 4.

⁷ Separate statement of FCC Commissioner Kathleen Abernathy, Memorandum Opinion and Order in CC Docket No. 96-45, released January 22, 2004.

1 Simply put, wireless ETCs can avoid providing service to customers in their designated
2 service areas if the cost of providing the service is unreasonable.⁸ That's why the jointly
3 filed revisions give the Office of Regulatory Staff the responsibility of determining
4 whether a request for service is unreasonable.

5
6 *But from an economic standpoint isn't the whole idea behind universal service support to*
7 *provide dollars to carriers serving areas where the costs of providing service are very*
8 *high; that is, where the costs are "unreasonable"?*

9
10 Yes it is. Universal service support is intended to keep the supported services affordable
11 in high-cost areas. That is the reason support is provided to high-cost areas (as opposed
12 to all areas) in the first place. The question that Embarq would put to the Commission is:
13 Is it in the public interest to allow C-ETCs to receive high-cost support but avoid serving
14 customers within their service area just because the costs are too high? Embarq would
15 strongly suggest that it is not. Yet that is allowed under what Alltel has described on
16 page 8 of their application when they indicate they will follow the steps that are outlined
17 in §54.202 of the FCC's rules.

18
19 The second issue the Commission should consider is that under existing FCC rules if an
20 ETC application is granted, the ETC will be under no obligation whatsoever to take USF
21 dollars and use them to expand its coverage into un-served or underserved areas.

⁸ See 47 CFR 54.202.a.1.i.B

1 *But doesn't Alltel, in its application, talk about a five-year build-out plan that it will*
2 *provide to the Commission that will describe, in detail, how it expects to expand its*
3 *coverage?*

4
5 Not exactly. In the application Alltel does say the following:

6 Finally, Alltel also commits to annually provide the Commission a progress report
7 consistent with §54.209(a)(1) of the FCC's rules. Alltel's plan will constitute a
8 good faith estimate of the universal service benefits—due to expanded coverage
9 and improved signal and service quality—that customers in the state of South
10 Carolina will enjoy...”
11

12 This sentence suggests (but does not guarantee) that Alltel will use USF dollars to expand
13 its coverage. However, in §54.209(a)(1) of the FCC's rules it clearly states that the
14 above-mentioned plan should reflect how universal service dollars were used to improve
15 signal quality, coverage or capacity. What this means is that Alltel could take every
16 dollar of USF support it receives and spend it on increasing the capacity of its towers in
17 downtown Columbia and Hilton Head, never spend a dollar expanding its coverage into
18 un-served areas, and still be completely consistent with §54.209. Again, Alltel's
19 application was filed pursuant to FCC rules, not the jointly filed revisions for South
20 Carolina ETC regulations.

21
22 So the second question that Embarq would put to the Commission is this: Is it in the
23 public interest to grant a C-ETC application knowing that the company is under no
24 obligation to use the dollars it received to expand its coverage? Without at least minimal
25 provisions like those contained in the jointly filed revisions, Embarq would strongly
26 suggest that it is not.

1 It is important to note that neither of these concerns is specific to Alltel's application or
2 even Alltel itself; rather, they are concerns regarding the overall C-ETC process and
3 existing obligations that C-ETCs have (or, more accurately, do not have). For example, it
4 is a fact if the application were granted as filed Alltel would be under no obligation to use
5 USF dollars to expand its coverage into un-served areas. Embarq's position is simply
6 that the FCC requirements that Alltel has agreed to meet, as outlined in its application,
7 are in and of themselves insufficient to ensure that the public interest will be served in
8 South Carolina. That is why Embarq—along with Alltel and the Office of Regulatory
9 Staff—has proposed revised guidelines that take steps toward addressing these issues.

10
11 *Please summarize your testimony.*

12
13 Embarq is not asking that Alltel's application be denied. Rather, Embarq is asking the
14 Commission to take additional steps—steps beyond those outlined in the FCC's
15 guidelines—to ensure that the public interest is served in South Carolina. Under existing
16 rules no C-ETC is required to use USF dollars to expand its network into un-served or
17 underserved areas, and under existing rules C-ETC can avoid serving certain customers.
18 Embarq believes that the public interest is better served by the Commission taking steps
19 to remedy these “loopholes” by 1) adopting the proposed guidelines discussed above, and
20 2) by moving toward greater regulatory parity among all ETCs (incumbent and
21 competitive).

1 *Does this conclude your testimony?*

2 Yes it does.

BEFORE
THE PUBLIC SERVICE COMMISSION
OF SOUTH CAROLINA

In Re:

Application of Alltel Communications,
Incorporated For Designation as an Eligible
Telecommunications Carrier Pursuant to Section
214(e)(2) of the Communications Act of 1934

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Docket No. 2007-151-C

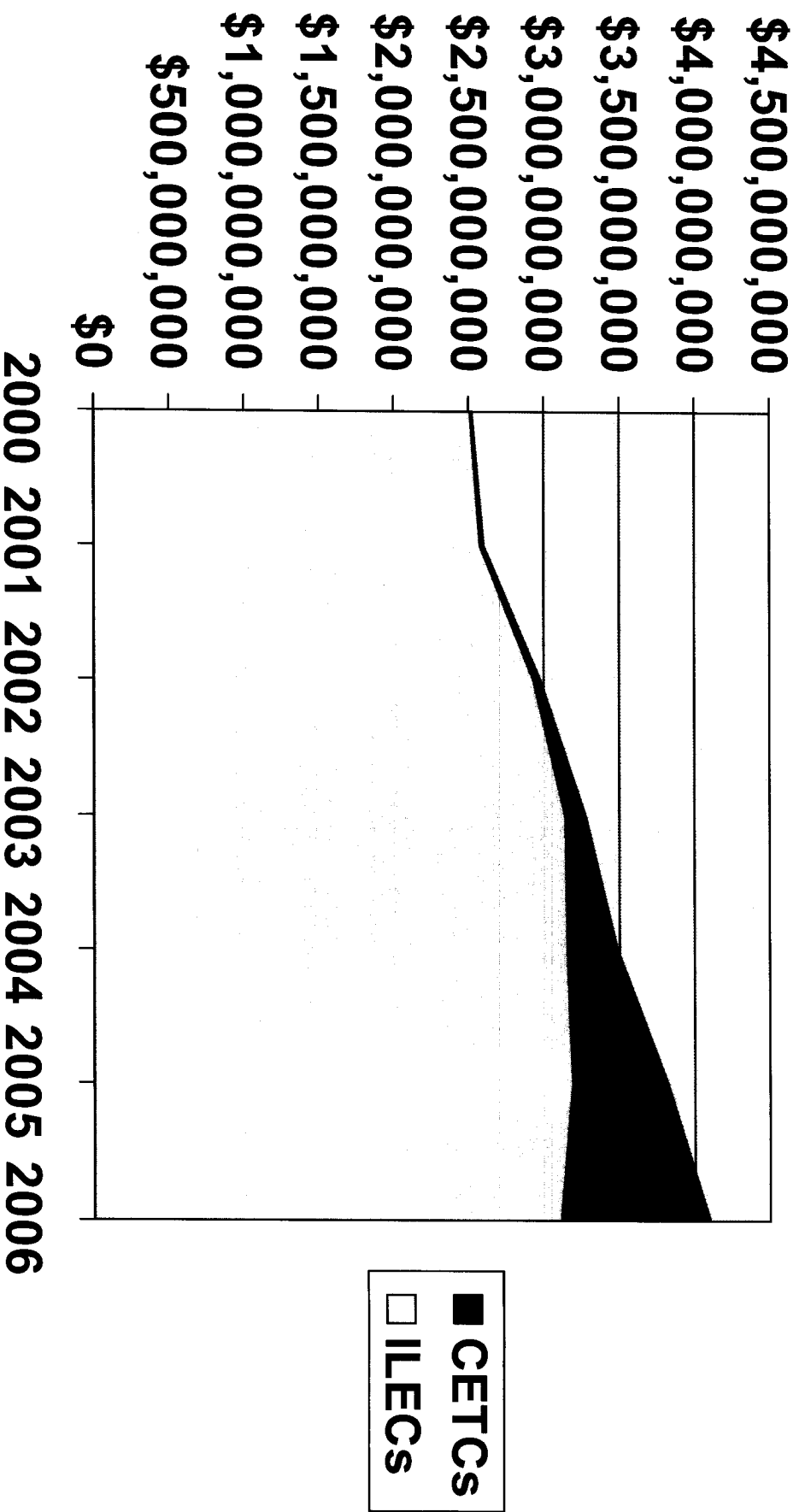
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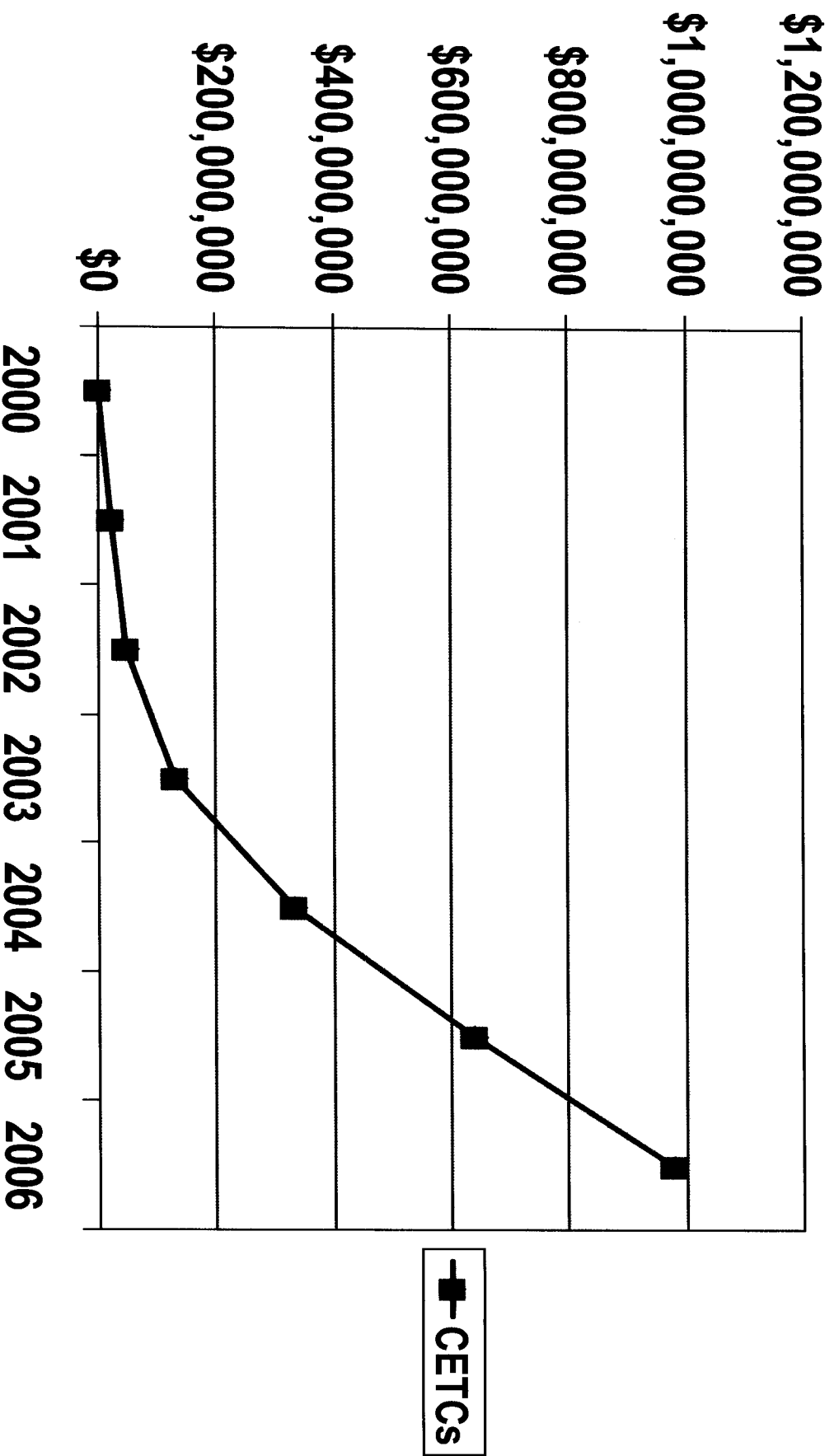
ATTACHMENT BKS-1

Total High-Cost Support Fund Payments – ILECs and CETCs



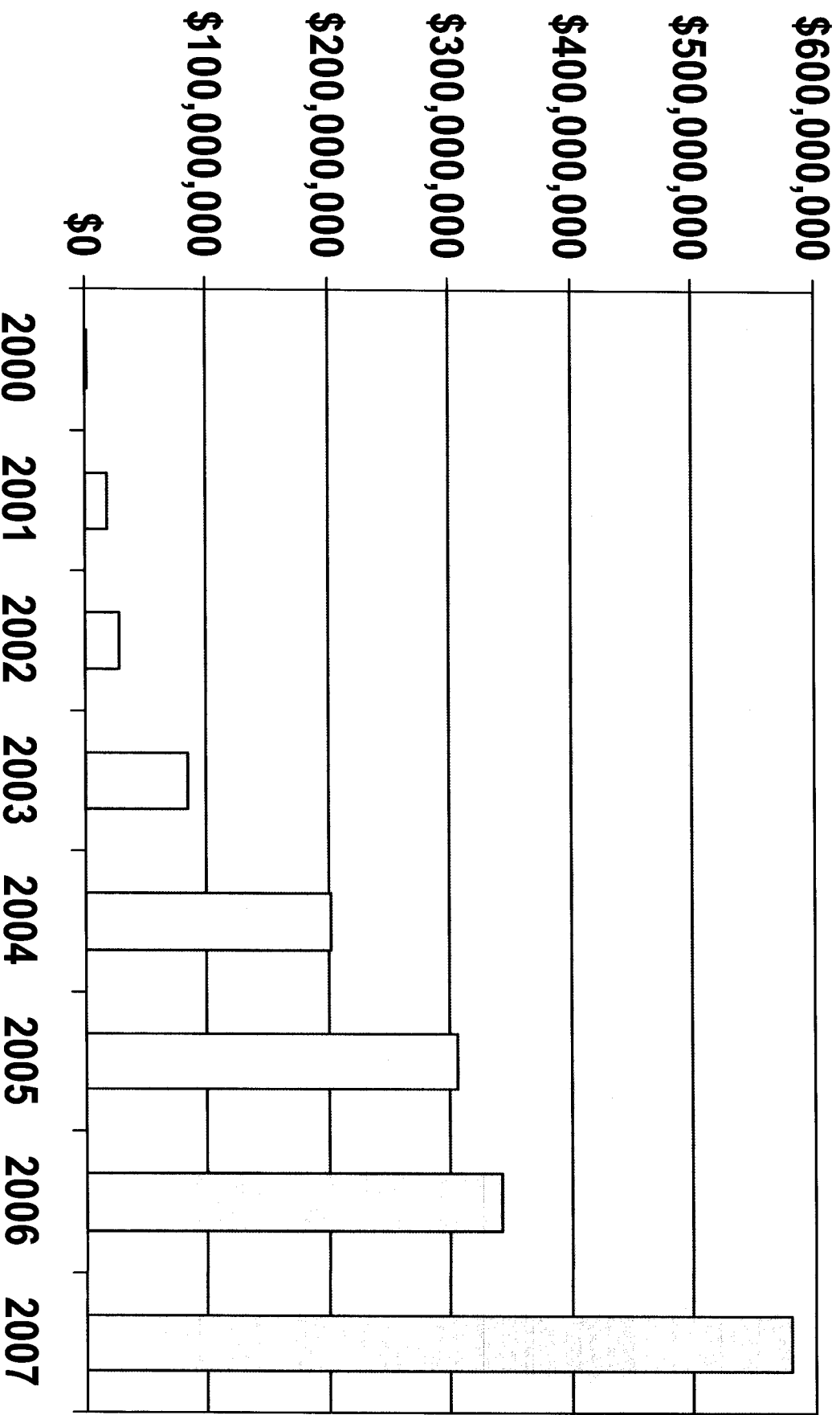
Source: USAC Data and Projections

Total High-Cost Support Fund Payments - CETCs



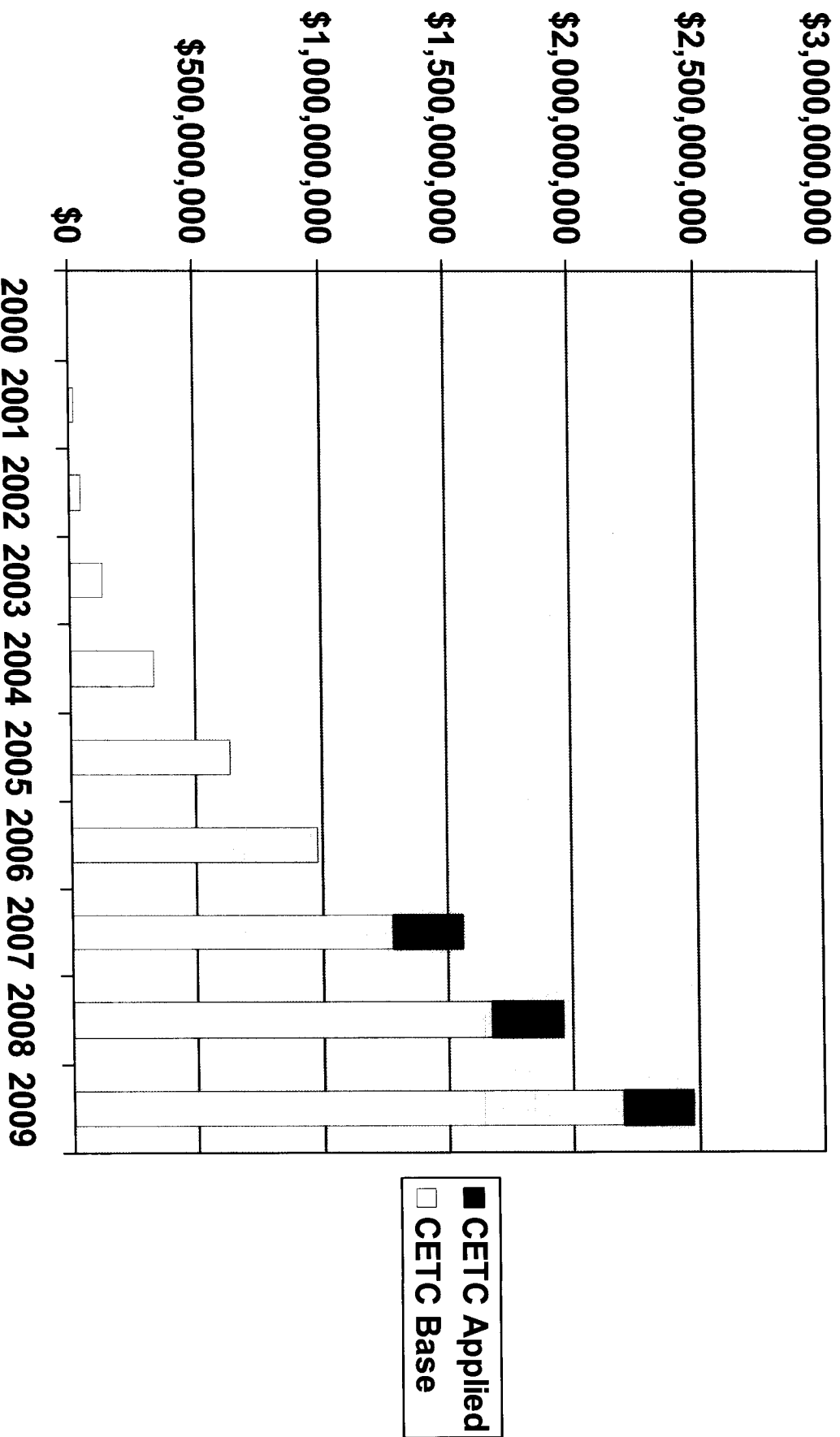
Source: USAC Data and Projections

CETC Dollar Growth



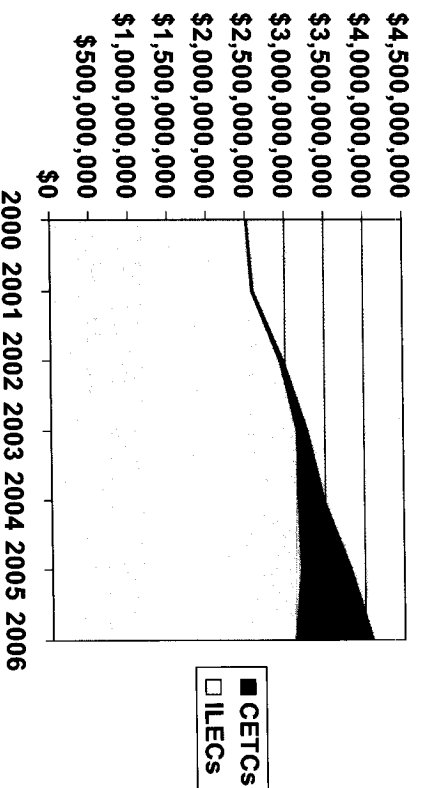
Source: USAC Data and Projections

CETC Disbursements

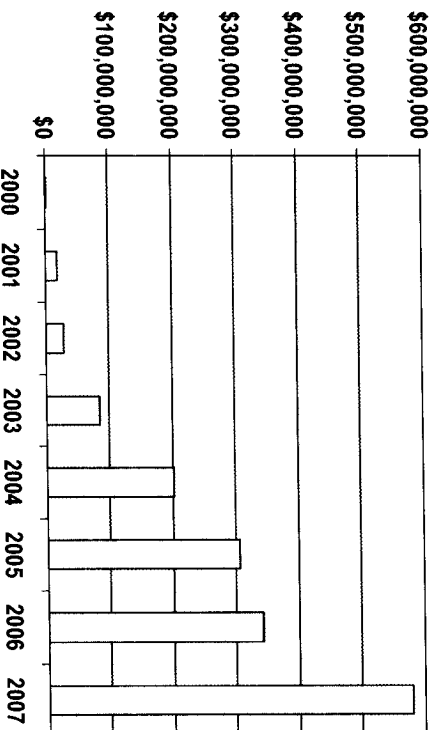


Source: USAC Data and USAC and FCC Staff Projections

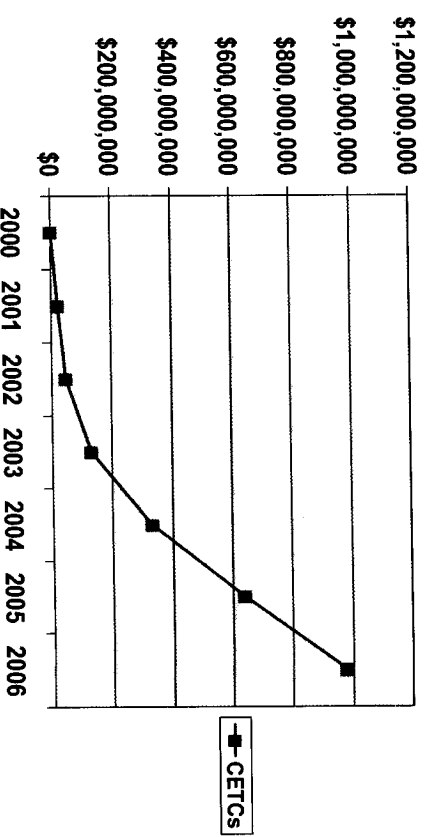
Total High-Cost Support Fund Payments – ILECs and CETCs



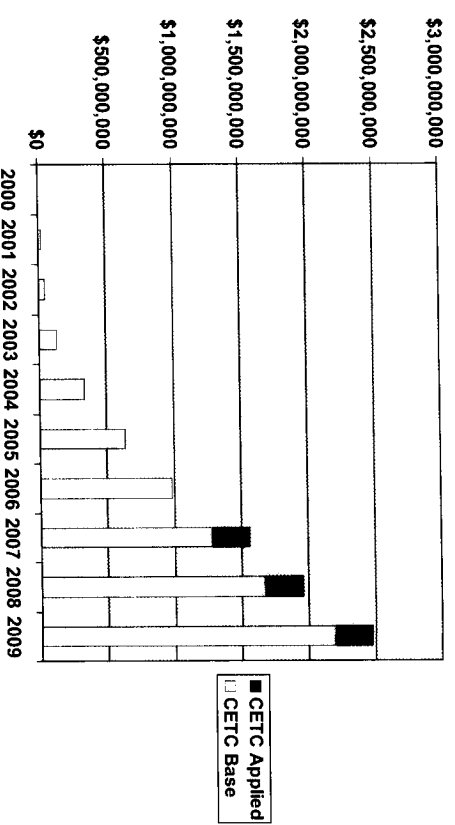
CETC Dollar Growth



Total High-Cost Support Fund Payments - CETCs



CETC Disbursements



CERTIFICATE OF SERVICE

The undersigned employee of Elliott & Elliott, P.A. does hereby certify that she has served below listed parties with a copy of the pleading indicated below by mailing a copy of same to them in the United States mail, with sufficient postage affixed thereto and return address clearly marked on the date indicated below:

RE: Application of Alltel Communications, Incorporated for Designation as an Eligible Telecommunications Carrier in the State of South Carolina

DOCKET NO.: 2007-151-C

PARTIES SERVED: C. Lessie Hammonds, Esquire
ORS
P. O. Box 11263
Columbia, SC 29211

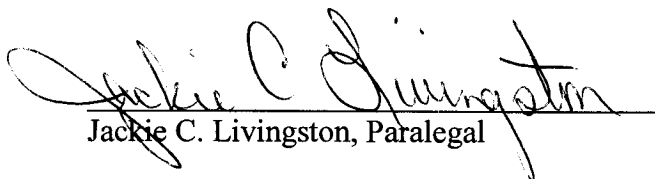
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PLEADING: Testimony of Dr. Brian K. Staihr

June 15, 2007


Jackie C. Livingston, Paralegal